Department for Business & Trade

HM Treasury

Long-term Investment for Technology and Science (LIFTS) initiative

Summary of responses

25 May 2023

Contents

Government response

The Government welcomes the positive response to its request for feedback on the Long-term Investment for Technology & Science (LIFTS) initiative from across the investment community.

We sought to understand the view of market participants, including potential LIFTS applicants, as well as a wider range of stakeholders, on the design of this initiative. We are encouraged to see that most respondents felt the options identified for LIFTS were appropriate and would be effective in meeting the programme's objectives. The responses have also provided useful insight and challenge on the proposed definition of 'qualifying investments', which the Government has reflected on. The LIFTS Call for Proposals is published separately by the British Business Bank (BBB) today. For all LIFTS related queries, please contact the BBB (LIFTS@british-business-bank.co.uk).

The Government has considered these responses and worked closely with the BBB to develop the design of the LIFTS initiative. As a result of the feedback received, the Government is proceeding with a Call for Proposals that includes the four options for government support provided in the consultation. We have taken this decision on the basis that there was support for all options, albeit to slightly varying degrees, amongst responses. This indicates that if some options were removed, there may be a risk that some potential applicants may not put forward bids and ultimately LIFTS may not meet its objectives. One minor change has been made regarding the BPC investment collaboration option, on the basis that this option was in practice a different proposition to the others. A decision has been made to position this differently within the CfP as an alternative option open to interested institutional investors but not one that will be formally assessed through LIFTS.

We have also taken the decision to modify the definition of 'qualifying investments' in response to feedback. We will set a minimum criterion of 50% UK content in the LIFTS fund(s), or 1x the HMG investment, whichever is higher, as respondents largely agreed that this was achievable and justifiable given HMG's policy objectives. However, the definition of science and technology firms will be made broader. This decision has been taken on the basis that respondents felt the proposed definition in the consultation document was too restrictive, and a broader definition would meet the diversification needs of potential applicants. However, we will make clear within the assessment criteria that applicants who can demonstrate a higher level of both UK and technology-focused investments will be scored more highly.

The Government also recognises that unlocking institutional investment, particularly DC pension capital, is a long-term policy area. Departments will continue to progress with work on the wider productive finance agenda, of which the LIFTS initiative is a part. The Chancellor will provide further statements on this agenda in the coming months.

The responses are summarised below. We have not attributed comments or views to individual respondents to ensure commercial confidentiality (a list of respondents is attached as an Annex). The summary of responses focuses primarily on feedback received from institutional investors and fund managers, given they are the target audience for the initiative. Where comments from trade associations or other organisations are deemed particularly relevant, we have referred to these directly.

In practice some respondents may fall into more than one category, however, they have been sorted according to the most straightforward definition. Where figures do not add up to the total number of respondents for a given organisation, it is due to non-response.

Summary of responses

Question 1: In your view, will the options for delivery be effective in achieving the LIFTS objectives? Please outline any adjustments to these options that you believe would increase their effectiveness.

Feedback on individual options is consolidated under question 2.

There is a broad consensus from the responses, across all organisation types, that the four options identified will be effective in achieving the LIFTS objectives. Respondents largely welcomed LIFTS as an innovative attempt to crowd-in institutional investment into UK Venture Capital (VC). However, views about which options might be most effective ranged widely both across and between the audience segments.

Institutional investors broadly agreed that the options would be effective but differed on which ones might provide the clearest incentive. For instance, across the nine respondents in this category, each of the four options was selected at least once as the most impactful form of support. Pari passu co-investment was selected four times, as was the capped returns option, followed by fee offset mechanism (three times) and BPC investment collaboration (three times). The fee offset option generated some strong views; three institutional investors felt it would be the most transformational while others, though understanding its inclusion, felt it would be unsustainable and set the wrong incentives.

Fund managers (including VCs and investment companies) also broadly welcomed the LIFTS options but, like the institutional investors, varied in their views on particular options. Noting that most respondents selected more than one option, of the sixteen respondents in this category the leading option identified was pari passu co-investment (option 2) selected by eight fund managers. However, there remained interest in the fee offset and capped returns options (selected four times).

There were divergent responses from fund managers on the two potential 'subsidy' options, the capped returns co-investment and fee offset mechanism. Options 3 and 4 were cited by some as adjusting the risk-return profile in a more meaningful way that would entice pension fund capital; however this view was not uniformly shared. A handful commented that, though welcome, options 1 (investment collaboration) and 2 (pari passu co-investment) would be unlikely to generate the scale needed to make a significant impact.

Other comments

There were a number of recurring comments and broader observations across the responses, including from non-investor respondents (i.e. trade associations).

First, several respondents proposed that the financial support available could be used – either via the LIFTS initiative or through a separate mechanism – to seed a privately-run fund-of-funds vehicle. The rationale for this is that it would provide a vehicle of sufficient scale and allow diversification across multiple different fund managers. This would fall under option 2 (pari passu co-investment). The Government believes such an approach would still be compatible with the LIFTS initiative, provided a proposal was submitted on these lines that met the required criteria. Given it was independently raised by several respondents, we have ensured the Call for Proposals makes clear that this would be a viable delivery option.

Second, several respondents reiterated the real or perceived barriers facing institutional investors when considering allocating capital to VC. Consistent with other Government taskforces and industry reports, constraints around liquidity, fees and a lack of education or expertise were cited as obstacles. Respondents noted that LIFTS would be successful if Government can demonstrate convincingly that it forms part of a wider, coherent package of reforms aimed at unlocking institutional investment. In addition, culture and education were frequently raised and it was suggested that Government should play a facilitating role in bringing different parts of the investment community together. While recognising the importance of these points and their interdependency with the LIFTS initiative, we are taking action to address many of these points separately through other initiatives led by HM Treasury and the Department for Work & Pensions (DWP), and as such these comments are largely out of scope for this consultation.

Several respondents stated that VC investment remained too risky a proposition for pension savers and reiterated the reputational and financial risks of facilitating too hasty a move into this area. Other observations received included suggestions such as tax incentives or loss relief (i.e. a government guarantee) on VC investments. The LTAF was also cited a handful of times as the appropriate investment vehicle for LIFTS funds. Finally, a number of comments were also made about the scale of the proposed £250m investment and whether this would be enough to meet demand.

Question 2: Which option, or combination of options, would your organisation be most interested in if you were to put forward or support a proposal in due course?

As noted above, organisations (specifically institutional investors and fund managers) indicated a preference for a range of different options. Across these two groups, each option was selected at least once. There was, on balance, a larger number of organisations who identified option 2 (pari passu co-investment) as the one they would be most interested in. However, this was often chosen in combination with other options. In addition, although the fee offset mechanism and capped returns options generated some divergent views, they were nonetheless seen as highly important to several respondents and the option that they would choose if they were to take forward a proposal.

Consultation responses against each option are summarised below, as we have noted general preferences in the question above.

Option 1 – BPC investment collaboration

This was identified as a preferred option by five institutional investors and/or fund managers that responded.

The main reason given for why this might be attractive included the prospect of benefitting from BPC's expertise and role in the market. It was noted by several respondents that this option would be better suited (and therefore most attractive) to small funds without much scale or expertise in the asset class.

However, some respondents felt this offer would not be attractive to DC pension funds as it would not meaningfully adjust the risk-return profile of VC investments. It was also noted that this option might not provide a solution 'at scale' to unlocking institutional investment.

Option 2 – Pari passu co-investment

This was identified as a preferred option by twelve institutional investors and/or fund managers that responded.

Respondents who selected this option felt it was the least complex option and could help ensure that the interests of all investor parties were aligned. Respondents also stated that the presence of a government financial commitment would also help to provide some certainty and de-risk the investment proposition. It was noted that this option would also be a more sustainable option than others (namely the capped returns and fee offset models). A handful of respondents felt this option might be most effective as part of a fund-of-funds proposal, with government effectively providing seed capital that then leveraged in pension fund commitments.

However, some respondents felt that the main drawback of this option is that it would not move the dial sufficiently. It was argued by some that it would not fundamentally change the risk-return profile of the asset class for pension funds and was unlikely to lead to a serious shift in investment on its own.

Option 3 – Capped returns co-investment

This was identified as a preferred option by seven institutional investors and/or fund managers that responded.

This option received support due to the fact that it provides DC schemes and fund managers with more upside from potential investment returns. This was felt to be helpful to DC schemes, in particular, for making the risk-return profile of the asset class more attractive.

However, some felt this option would not be effective. Reasons given include that pension funds' main concern with the asset class is more related to up-front costs (especially fees) than generating significantly higher returns; and also that it would set an unsustainable precedent for the role of government support in investing in VC. Some respondents also said that its strength as an incentive would ultimately depend on the terms of any agreement with government.

Option 4 – Fee offset mechanism

This was identified as a preferred option by eight institutional investors and/or fund managers that responded.

The fee offset option generated the most divergent opinions across the range of respondents. Some felt that this would be the most transformational option, as it directly addressed a commonly cited barrier to DC pension involvement. However, it was also suggested it would not be suitable for UK DC schemes or the long-term sustainability of VC investing, given it risks creating an artificially low price for asset management.

Question 3: Do you agree that a requirement to invest at least 50% of the proposed fund or structure into qualifying investments would be a suitable minimum threshold for proposals? If not, what alternative threshold would you propose that would achieve sufficient focus on UK science and technology companies?

There was broad agreement across respondents that at least 50% of the proposed fund or structure into 'qualifying investments' (namely UK-based science and technology firms) would be a suitable minimum threshold. Respondents understood that the commitment of government capital would entail some expectations on this point, indeed some suggested the thresholds be set significantly higher, but many also noted there may be a need for pragmatism and flexibility.

Three institutional investors were content with the proposed structure. Two suggested minor modifications, such as separating the UK-based requirement from the science and technology one at different levels to enable more diversification; or adjusting the thresholds depending on whether HMG investment was pari passu or sub-ordinated. One institutional investor suggested a lower threshold (two others did not answer).

All fund managers who responded to this question (fourteen) said they were content with the proposed 50% threshold. Several (five) said the threshold was too low and advocated for a higher figure.

Lastly, several respondents suggested government should be pragmatic when considering how such thresholds should be measured in order to minimise restrictions on investment strategy and running a fund (for example, measuring such thresholds at the time capital is deployed, not requiring ongoing assessments). Similarly, it was suggested by one respondent who disagreed with the 50% requirement that government should adopt a principles-based, rather than target-based approach, to avoid being overly restrictive.

Question 4: Do you agree with the proposed definition of qualifying investments? If not, what alternative definition would you propose that would achieve sufficient focus on UK science and technology companies?

Respondents provided a much greater range of answers regarding the proposed definition of qualifying investments that was outlined in the request for feedback document. A number of alternative definitions were proposed.

For institutional investors that responded to the question, most (five) broadly agreed with the proposed definition.

However, views were much more mixed amongst fund managers. A majority (nine) did not agree with the proposed definition or suggested major revisions. The primary reason given was that the definition was simply too tightly specified and therefore burdensome. Those that were broadly supportive (four) also indicated minor tweaks. Suggestions for different definitions also did not command a consensus. Some respondents also felt the definition was too skewed towards early-stage companies and suggested altering the R&D spending requirement to take more account of scale-up firms; others felt the employment (headcount) measure was insufficiently flexible. Other ideas were to adopt the definition of 'knowledge-intensive' businesses as per HMG tax relief definitions.

Question 5: How likely is your organisation to put forward a proposal in due course, either individually or in collaboration with others? If relevant, please summarise any changes that would make your participation more likely.

Several respondents across the institutional investor and fund manager categories indicated that they would expect to put forward proposals, including in collaboration with others. However, to avoid any risk of prejudicing the eventual LIFTS initiative once established, we have chosen not to reveal the number, or names, of these respondents.

Annex: Respondents

Organisation	Count	Respondents
Institutional investor	9	Aegon, Aviva, Smart Pension, Legal & General, Mercer, M&G, Imperial College London, Scottish Widows, Phoenix Group
Fund manager / VC / Investment company	17	Beringea, Bioscience Managers, Cambridge Innovation Capital, Crux Asset Management, Downing LLP, Glen Partners, Longwall Ventures, Midlands Mindforge, Molten Ventures, Octopus Group, Oxford Science Enterprises, Panmure Gordon, Schroders, IFM Investors, IP Group & Parkwalk, SV Health Investors, ICG PLC
Investment consultant / lawyers	5	Northeast Capital, BOOST consortium, Simon Wiles, Lane Clark and Peacock LLP, Simmons & Simmons
Trade association	7	Association of British Insurers, Association of Consulting Actuaries, BVCA, Pensions & Lifetime Savings Association, Scale-up Institute, Investment Association, Bio Industry Association

Other	3	Dan Mahoney (HMG Life Sciences Envoy), Hargreaves Lansdown, Unison
Total	41	

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